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A concise easily digested periodic analysis based upon scientific research in real estate fundamentals and trends. Constantly measuring and reporting the basic economic factors responsible for changes in trends and values.... Current Studies.... Survey.... Forecasts

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REAL ESTATE ECONOMISTS, APPRAISERS AND COUNSELORS

CONSTRUCTION COSTS REACH NEW PEAK

FOLLOWING their brief decline from their 1948 peak, construction costs are advancing again. The average cost of building our standard six-room frame house in 51 principal cities stood at $13,831 at the beginning of this year. The latest information from these cities indicates that the average cost is now $14,454, or 4.5% above the January figure. This latest amount is also $160 above the previous all-time peak of $14,294 reached in late 1948.

Although this general advance in construction costs has sprung directly from rising material (chiefly lumber and metal items) and labor costs, the underlying cause has been the extremely loose credit terms available to almost anyone who thought he might like to have a home. Under these circumstances rising production and rising sales prices are not surprising. Long-term amortization makes it possible to spread a price increase over 240 to 360 months and a $500 rise in sales

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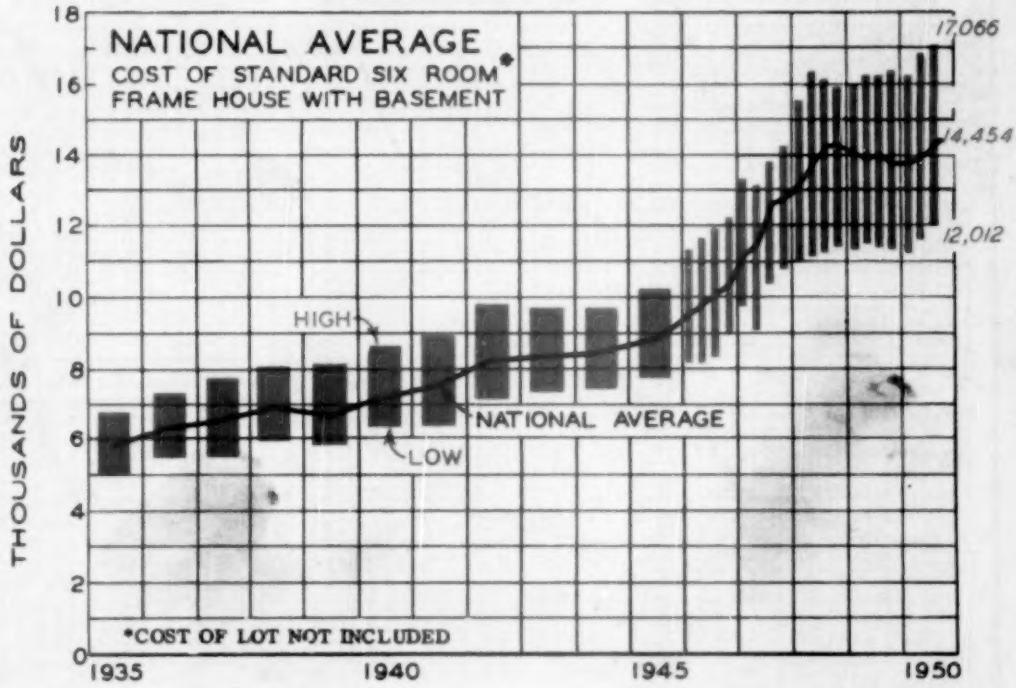

TOTAL CONSTRUCTION COSTS OF A STANDARD SIX ROOM FRAME HOUSE BY CITIES

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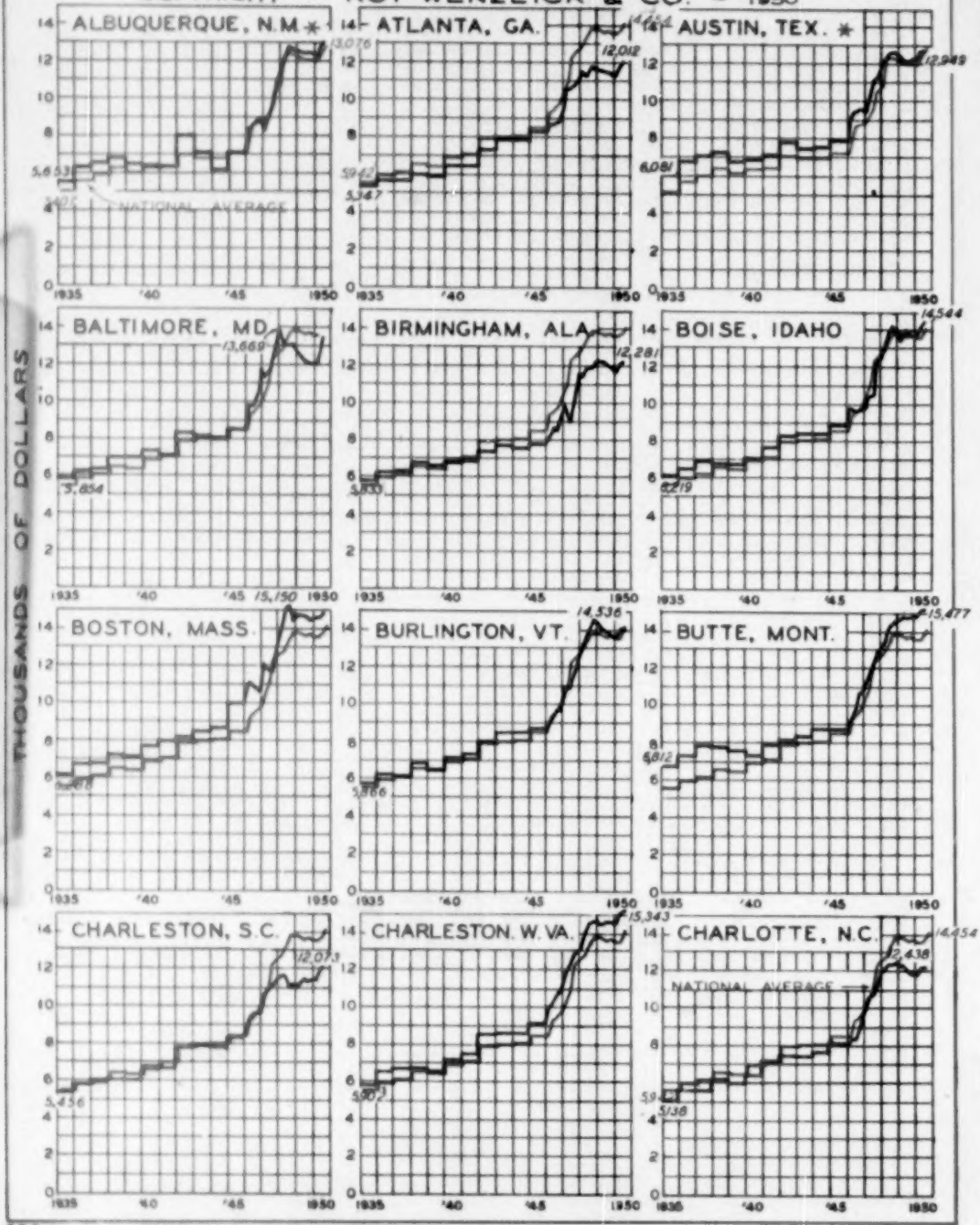

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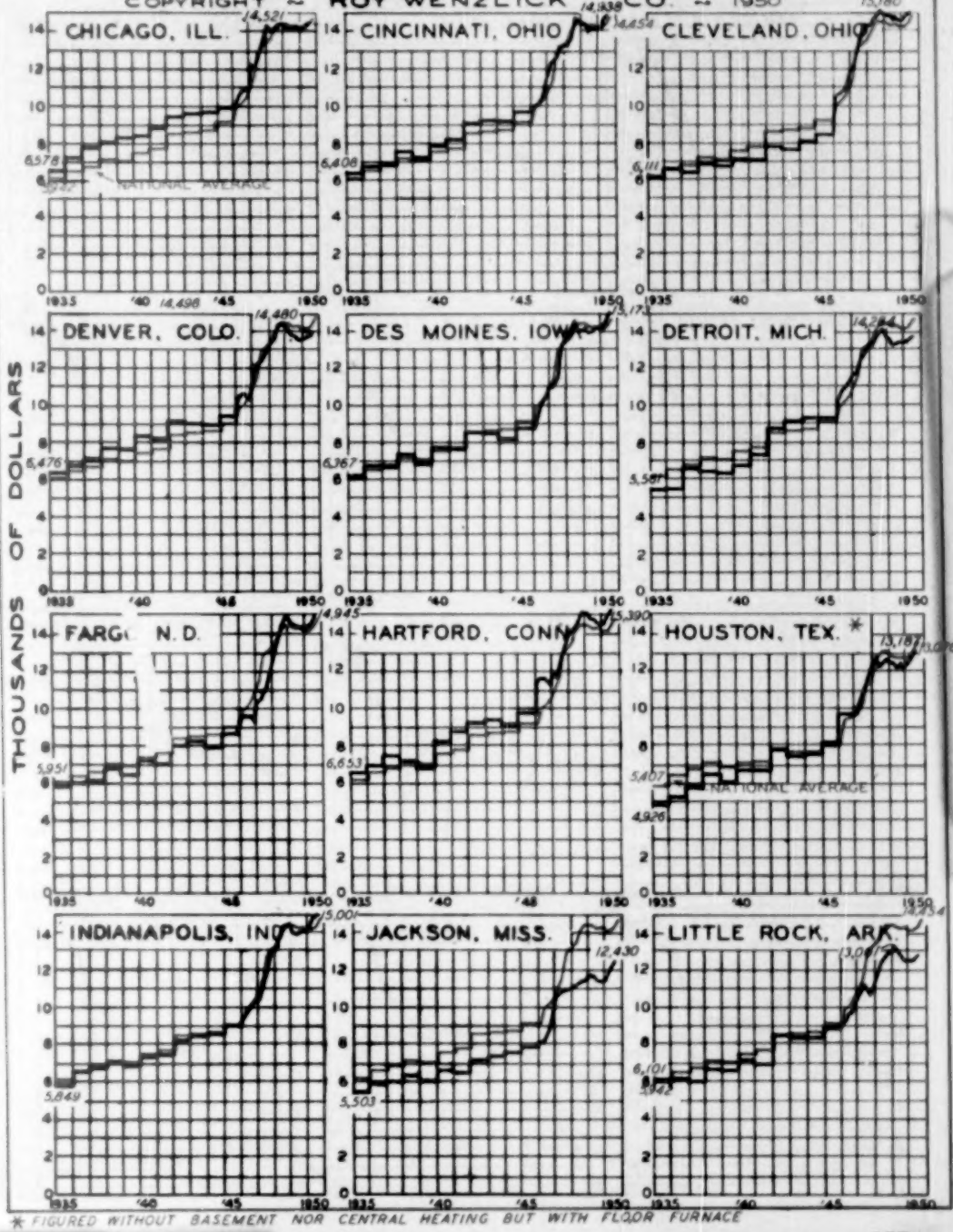
THOUSANDS OF DOLLARS



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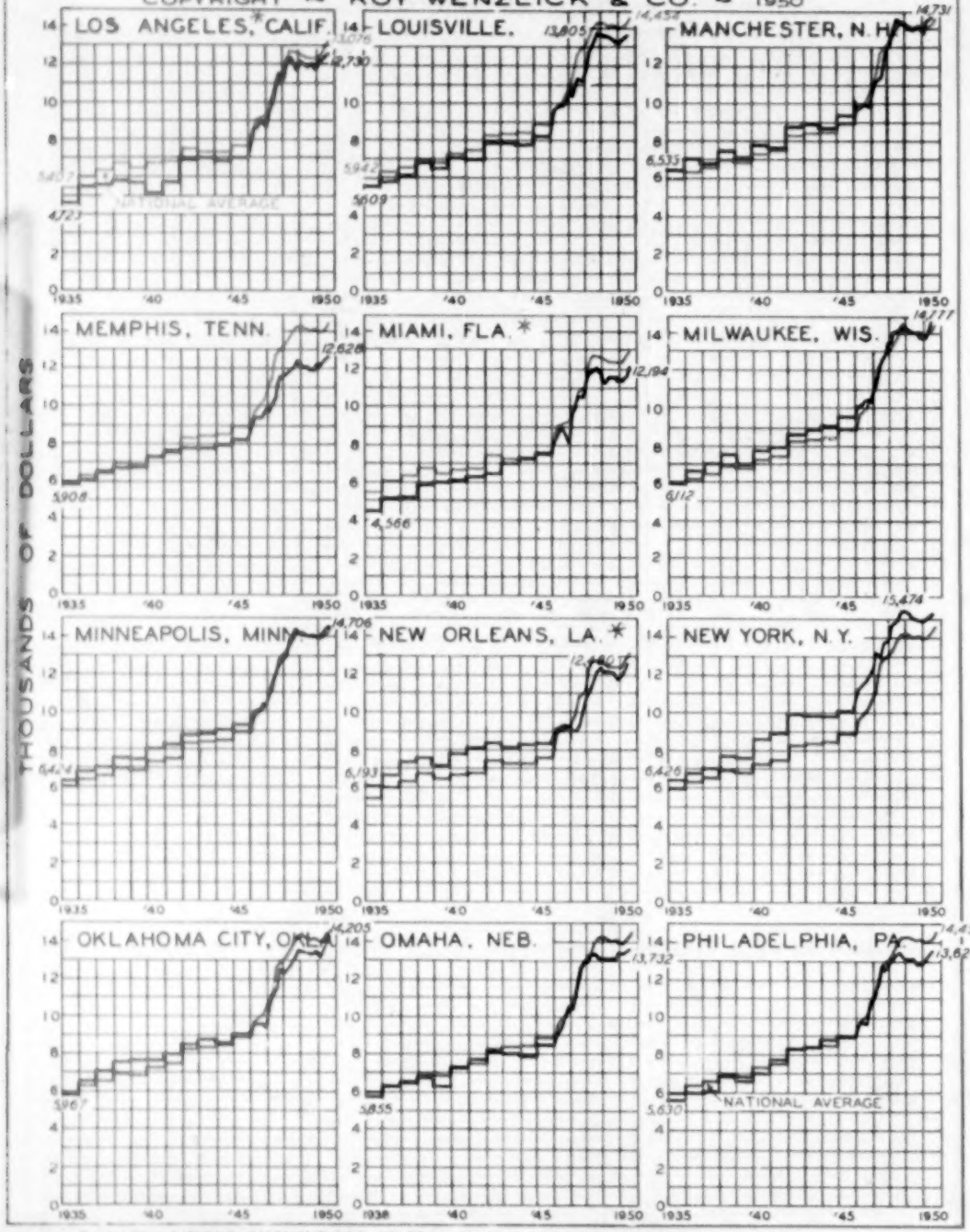

* FOR HOUSE WITHOUT BASEMENT NOR CENTRAL HEATING BUT WITH FLOOR FURNACE

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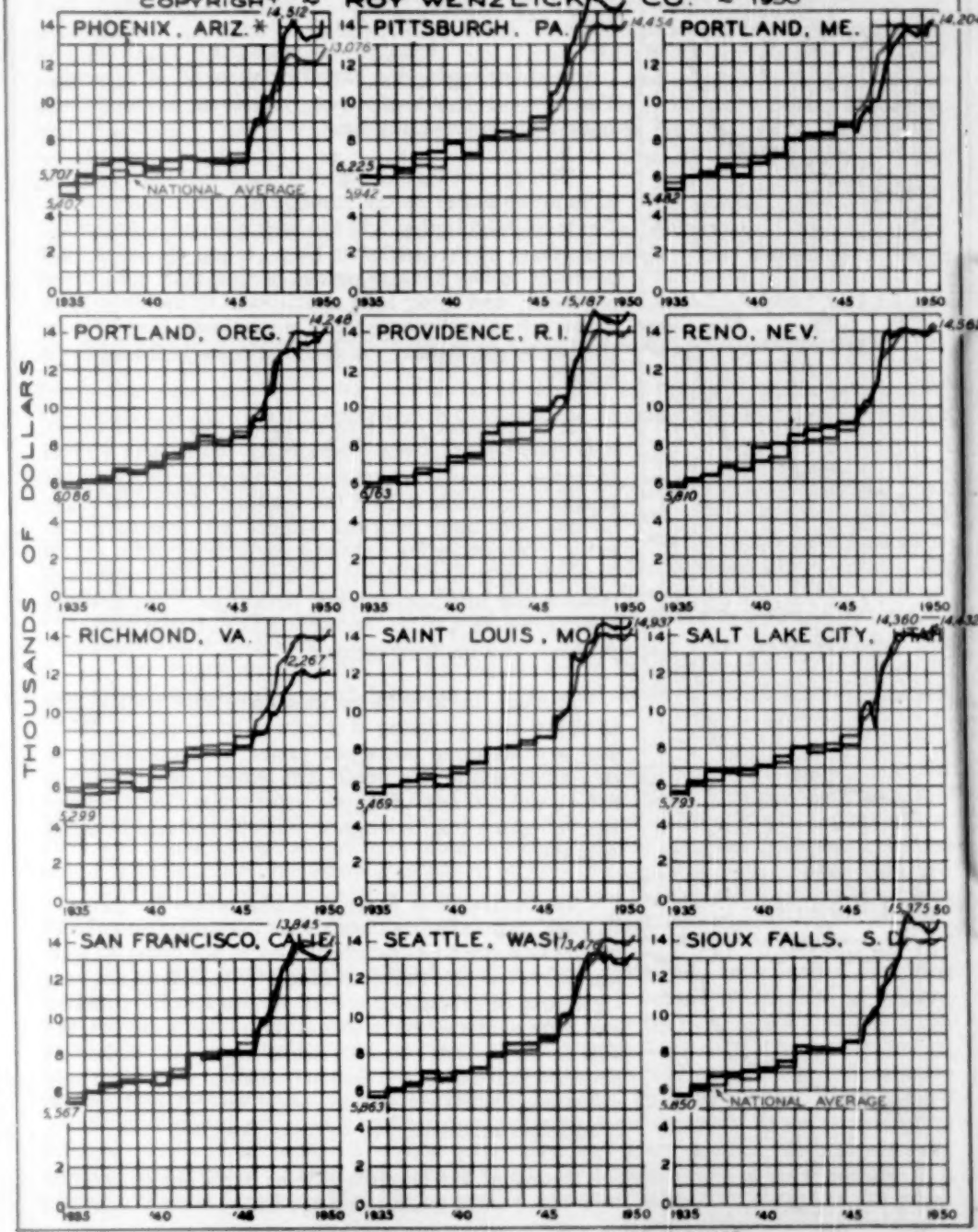

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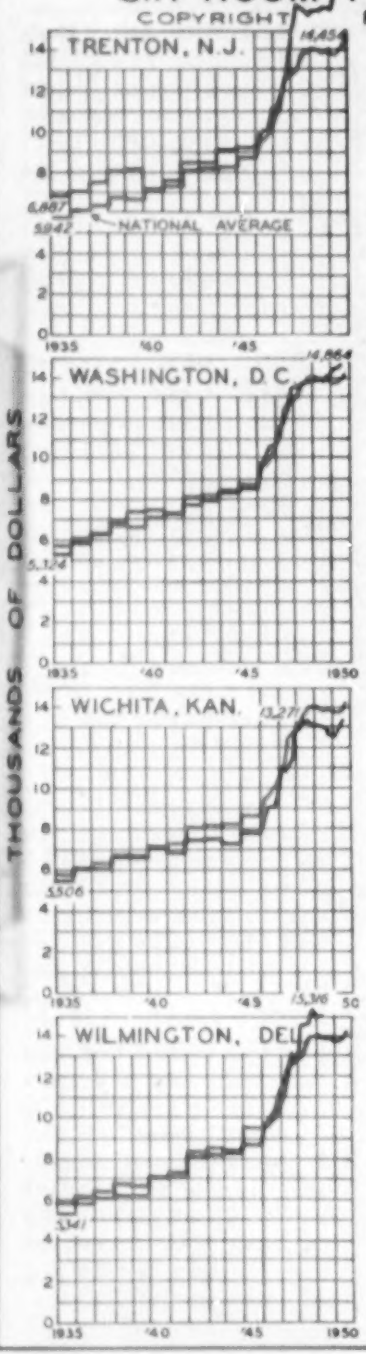


(cont. from page 355)

price means upping the payoff by about $3.00 a month. The low (or in some cases, no) down payment has been still more alluring.

The recent tightening of credit will undoubtedly have some effect on the number of homes purchased. Perhaps "tightening" is the wrong word. Actually, only some of the slack has been picked up. It is still possible to buy certain priced homes with a 5% down payment, and tying loan appraisals to the July 1950 construction cost means that the maximum loan is to be limited by the highest construction costs in the nation's history.

It is still too early to measure the effect of the new credit regulations. Naturally, there was a brief increase in construction and mortgage activity as attempts were made to beat the deadline of the new regulations, but their over-all effects will appear gradually. Obviously the primary purpose of these credit regulations is to cut down the amount of materials and labor going into non-defense buildings. The present arrangements will accomplish this to some degree - perhaps to a marked degree.

Through the first seven months of 1950 the building industry was operating at a rate of more than 1,440,000 new nonfarm units per year. A drop of 30% in this construction rate would still leave a rate of slightly over a million new units per year which, in our opinion, is more than enough to satisfy normal housing demand.

Therefore, our thought is that while the private builder will have his operations curtailed somewhat by the new credit regulations, he is not going to lose his market as the result of them. Whether or not real tightening of credit lies ahead, no one knows. Neither can it be said how much shrinkage in the home market will be the normal result of nearly five years of record production. So, home builders should stop worrying about their 1950 market and start worrying about the things that might happen to them later on.

On pages 356 through 360 we show the estimated

(cont. on page 361)

(cont. from page 360)

cost of building our standard six-room frame house from 1935 through the first half of 1950 in 51 cities. (Recent data on Wilmington, Delaware, have been unobtainable.) In 33 of these 51 cities, construction costs have already passed their former peaks. Washington, D. C., has shown the greatest rise over its 1948 peak with an increase of 6%. Jackson, Mississippi, and Portland, Oregon, costs are 5% above their former peaks. Oklahoma City is 4.7%, and Butte, Montana, and Charleston, South Carolina, are 4.5% above their former peaks. It is noteworthy that these rises are not concentrated in any particular section of the country.

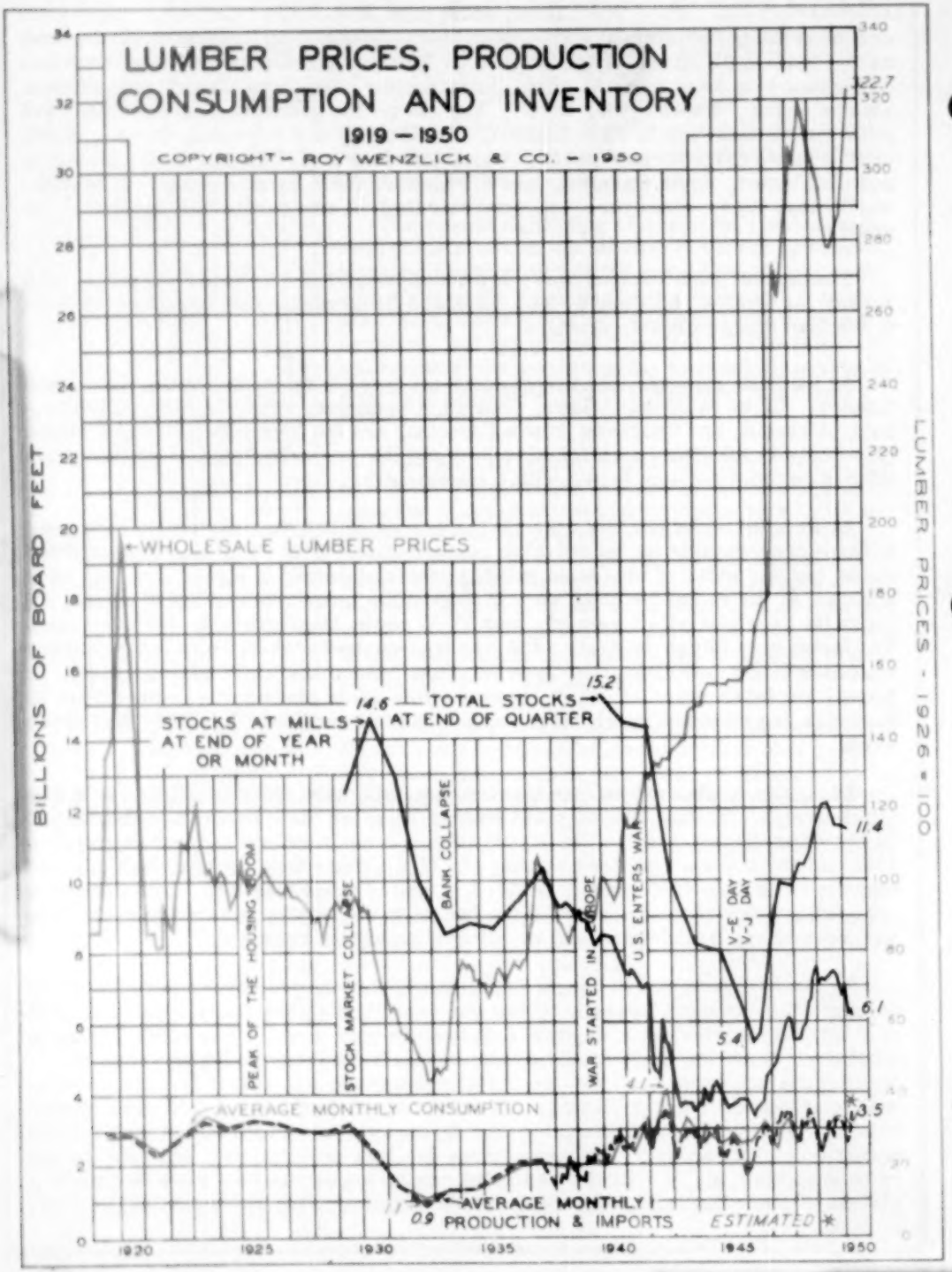
The highest construction costs are found mostly in the East. Trenton, New Jersey, is highest, followed by New York and Pittsburgh. One exception is found in the high costs in Butte, Montana.

As would be expected, the lowest costs are found in the southeastern part of the country. Of the 51 cities, Atlanta, Georgia, Charleston, South Carolina, Birmingham, Alabama, and Charlotte, North Carolina, are the four with the lowest costs. (The costs in all cities mentioned in this and the preceding paragraph have been figured on the six-room house with a basement.)

As we mentioned earlier, the rising prices of building materials have contributed considerably to record-high construction costs. The chart on page 363 shows that the index of wholesale building material prices is higher now than ever before. At the end of the first week in August the index reached 212.7 points, 4% above its previous all-time high, and 12½% above the August 9, 1949, reading. The latest rise began in early 1950 and was pushed steadily upward by rapidly expanding home building. On June 20, just before the start of hostilities in Korea, the index stood at 201.0, having risen 6% in six months. Since June 25 the index has climbed much faster and advanced another 6% in less than seven weeks.

Wholesale lumber prices (see chart on page 362) have likewise climbed to a new all-time high. By June 1950 they had risen to 1% above their previous peak of 319.5 (achieved in August 1948). The latest rise in lumber prices began in September 1949 and started from an index reading of 277.4. Since then the index has climbed steadily to its June 1950 reading of 322.7, a rise of more than 16%. Later data are not available but when the effect of the recent scare buying can be translated into index numbers, it will doubtless result in even higher readings.

Prices have been spurred onward since the first of the year by a record-breaking building rate and more recently by the war scare. It seems reasonable to believe that within a short while they should start down once more. The scare buying in most other fields has about run its course and the same thing should happen to building materials. Then, too, the new credit regulations will result in some curtailment of demand for materials to go into new homes. This should also work toward bringing prices down a bit provided new defense requirements do not pick up this possible slack in demand. Whatever price declines are realized, they are not apt to be breathtaking. About the best that can be hoped for is a slow decline to a plateau of about the same level these prices occupied in the early part of the year.


LUMBER PRICES, PRODUCTION
CONSUMPTION AND INVENTORY
1919 – 1950
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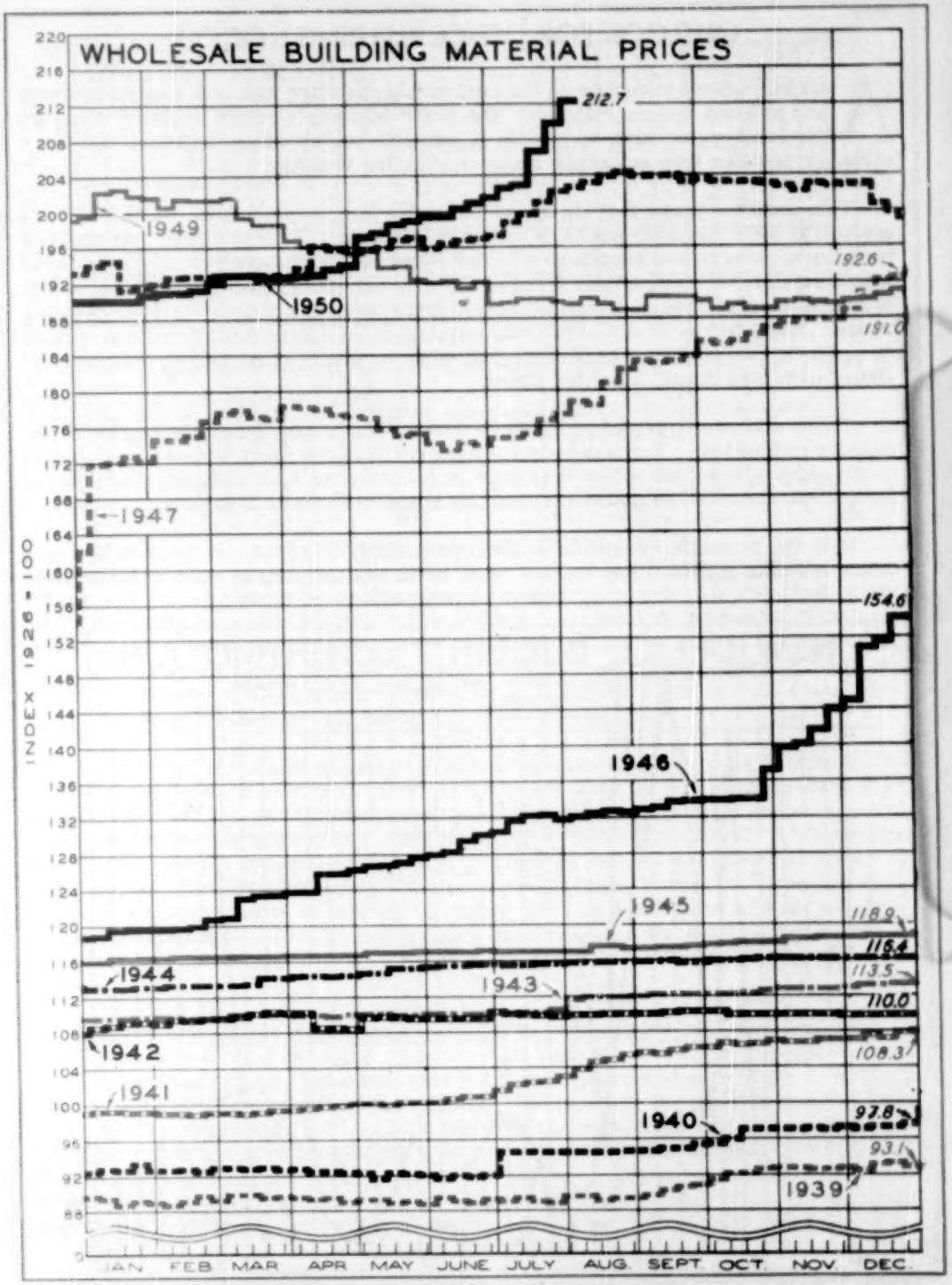
BILLIONS OF BOARD FEET
LUMBER PRICES - 1926 = 100
←WHOLESALE LUMBER PRICES
STOCKS AT MILLS AT END OF YEAR OR MONTH
14.6
TOTAL STOCKS AT END OF QUARTER
15.2
322.7
PEAK OF THE HOUSING BOOM
STOCK MARKET COLLAPSE
BANK COLLAPSE
WAR STARTED IN EUROPE
U.S. ENTERS WAR
V-E DAY
V-J DAY
11.4
6.1
5.4
4.1
3.5
AVERAGE MONTHLY CONSUMPTION
AVERAGE MONTHLY PRODUCTION & IMPORTS
1.1
.09
ESTIMATED *
1920
1925
1930
1935
1940
1945
1950


WHOLESALE BUILDING MATERIAL PRICES
INDEX 1926 - 100
220
216
212
208
204
200
196
192
188
184
180
176
172
168
164
160
156
152
148
144
140
136
132
128
124
120
116
112
108
104
100
96
92
88
0
212.7
1949
1926
1950
191.0
1947
154.6
1946
1945
118.9
116.4
1944
113.5
1943
110.0
1942
108.3
1941
1940
97.8
93.1
1939
JAN
FEB
MAR
APR
MAY
JUNE
JULY
AUG.
SEPT.
OCT.
NOV.
DEC.

OUTLOOK FOR OFFICE BUILDINGS GOOD

ALTHOUGH all branches of the real estate industry are faced with problems and plagued by uncertainties, the office building section probably occupies the least vulnerable spot. On a national scale, office buildings are in a stronger position than any other major part of the industry.

This does not mean that their position calls for complacency. Neither does it mean that their fortunate condition cannot deteriorate. In some cities, particularly New York, owners and managers of older office buildings have recently been faced with considerable competition from newly erected office space. Decentralization of downtown districts has brought actual and potential competition from outlying areas. Many business and industrial establishments have built new home offices in order to consolidate departments that were formerly scattered through several floors of rented downtown office space.

These different types of competition will naturally vary from one section of the country to another. For example, it appears that the most serious competition to the older Manhattan office buildings is found in the four million square feet of new, high-class office space that will be completed there this year.

With the possible exception of New York City, however, we believe that new office building construction will not be in sufficient quantity to offer serious com-

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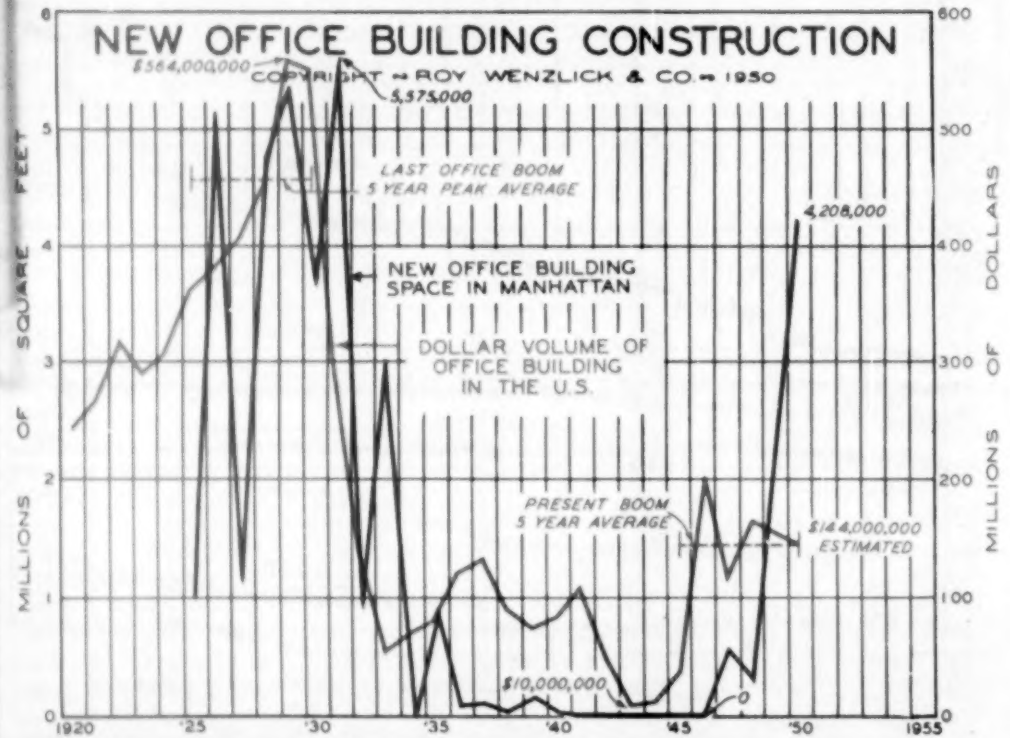
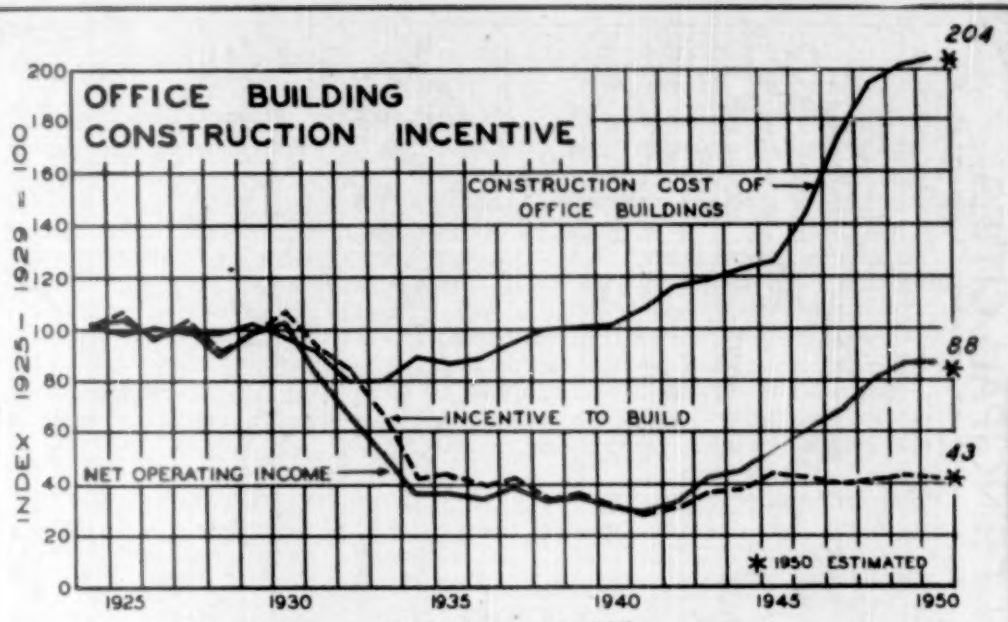




(cont. from page 364)

petition to existing properties for some time. Some new building will take place. There will nearly always be some cities where additional space is required, there will frequently be some organization willing to erect a monumental structure, and there will continue to be business establishments that desire to consolidate their rented space into a new and modern home office building. During the present boom, however, the amount of office building construction has not even begun to approach the amount put up during the 1925-1930 period.

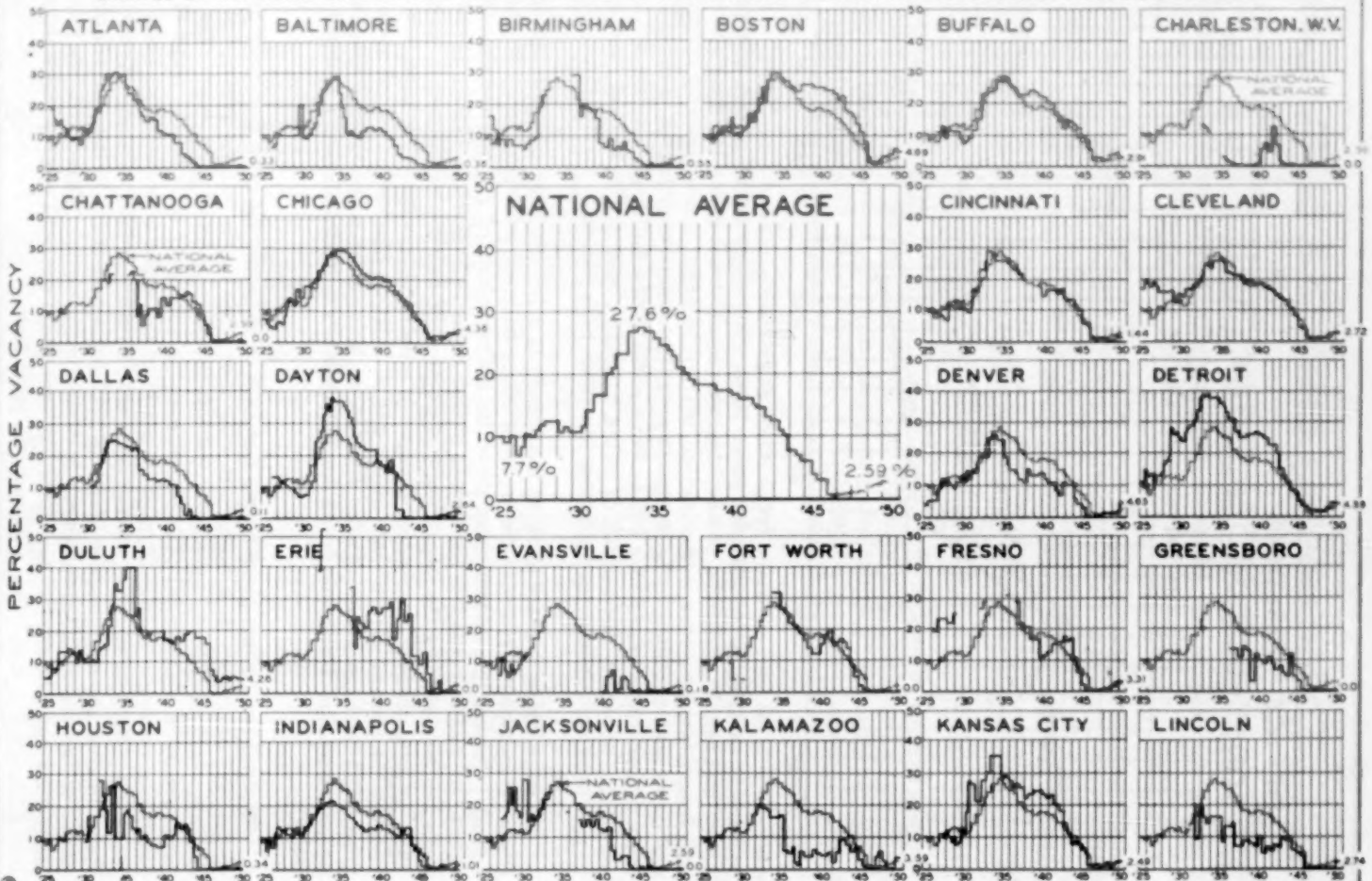
On page 364 is a chart showing the trends in office building construction in the United States compared with the trend of office building construction on Manhattan Island. The red line on this chart shows the dollar volume of all loft, warehouse and office buildings erected in the United States from 1920 through 1950. These figures are furnished by the Department of Commerce and are expressed in terms of 1939 dollars, thereby eliminating changes in construction costs. The blue line represents the square feet of new office space built on Manhattan Island each year from 1925 through 1950. These figures on Manhattan were taken from a chart prepared by Lee Thompson Smith for SKYSCRAPER MANAGEMENT (August 1950 issue).

The red line on this chart shows that 1926 to 1930 was the peak five-year period in the last office building boom. During that time there was an average of $469 million worth of offices, warehouse and loft buildings erected each year. The peak year was 1929 with a total of $564 million. In contrast, the present boom (1946-1950) has averaged only $157 million worth of the same type buildings each year. Thus far, 1946 has been the postwar peak with a figure of $204 million. Remember, these figures are expressed in terms of 1939 dollars in order to take the rubber out of the dollar and eliminate changes in construction costs. Therefore, we see that during the peak five-year period of our last boom we built nearly three times as

(cont. on page 369)

OFFICE BUILDING VACANCY IN PRINCIPAL CITIES

CHARTED BY ROY WENZLICK & CO. FROM DATA FURNISHED BY THE NATIONAL ASSOCIATION OF BUILDING OWNERS & MANAGERS



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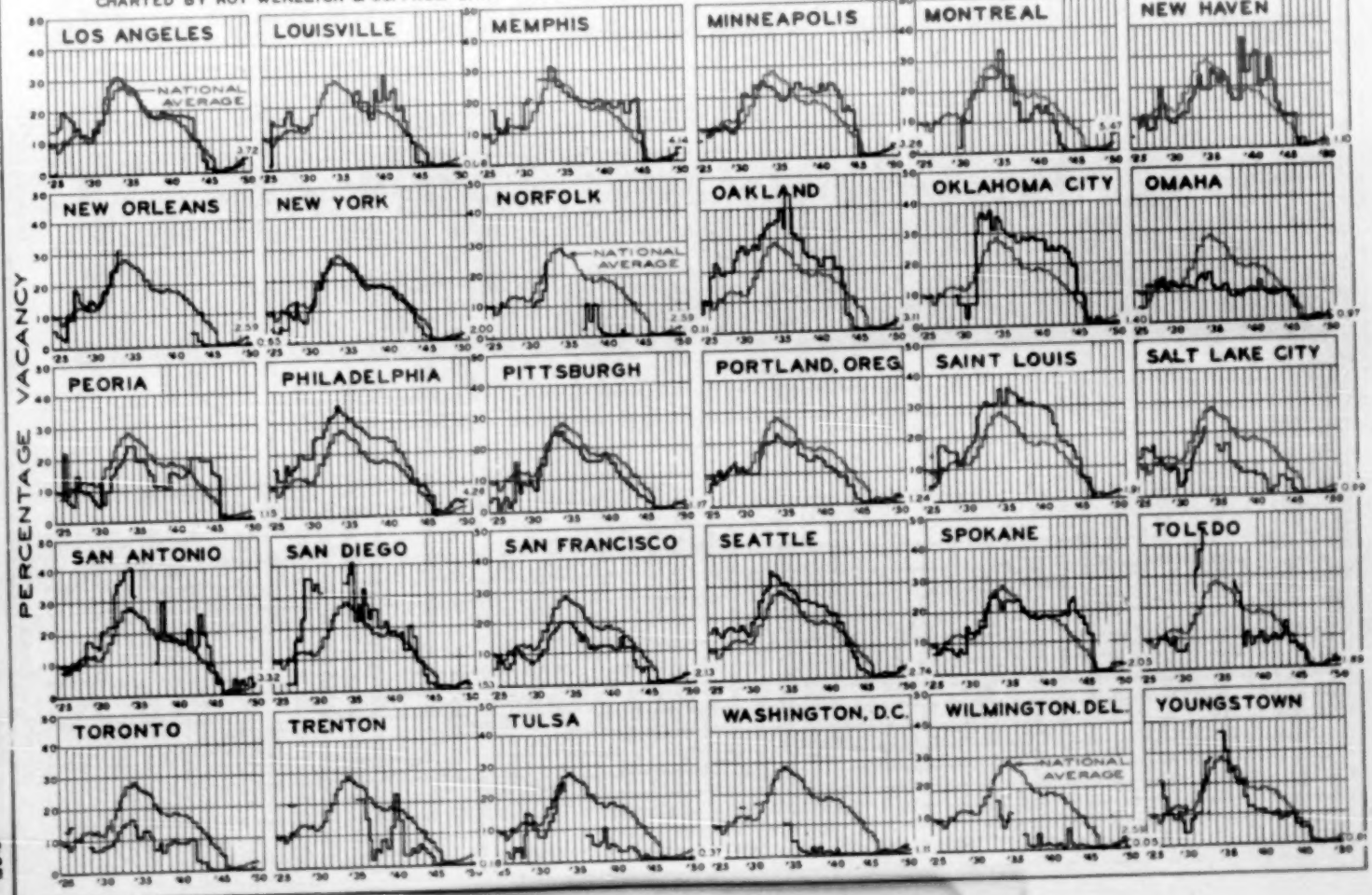
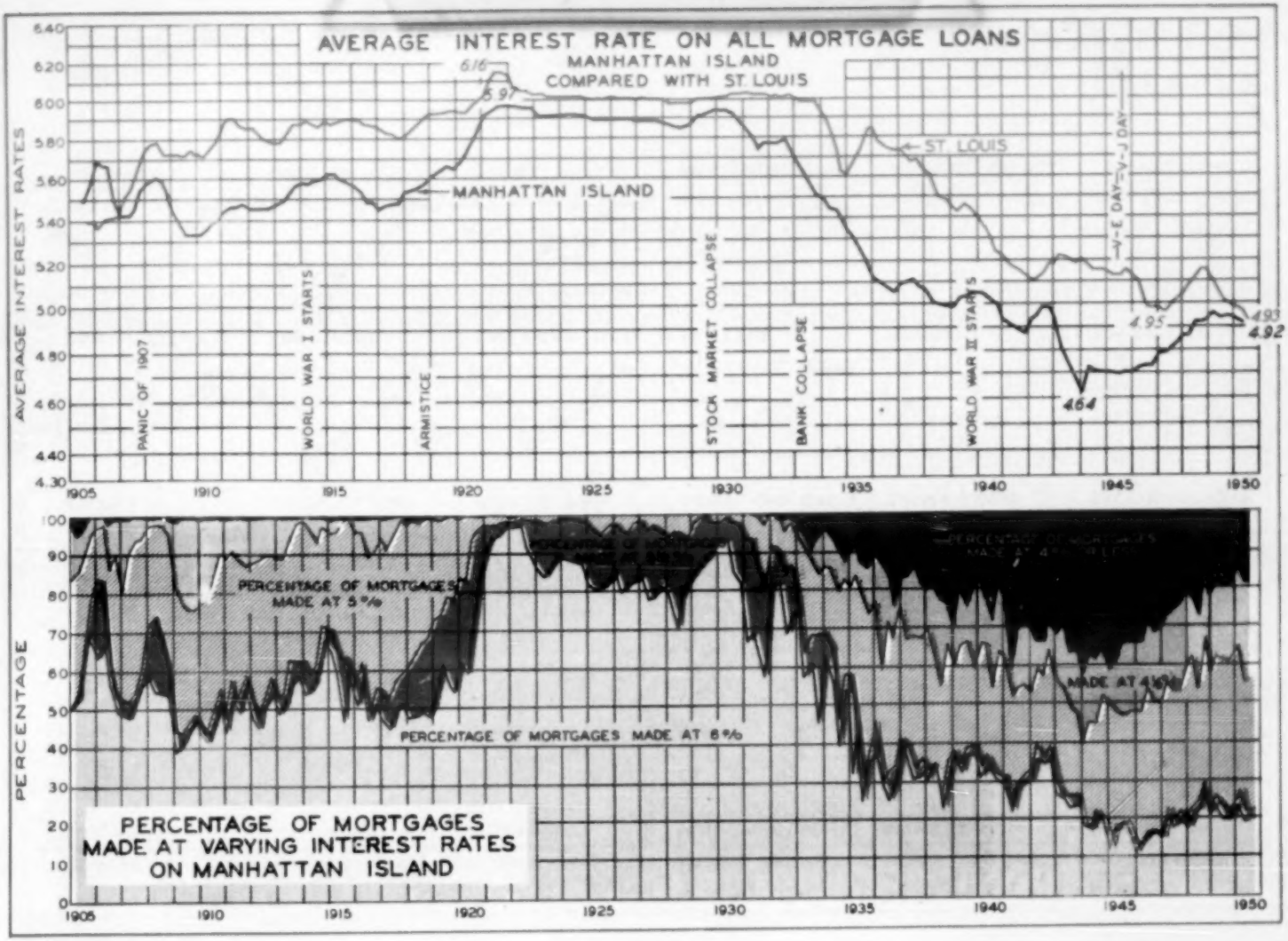
OFFICE BUILDING VACANCY IN PRINCIPAL CITIES

CHARTED BY ROY WENZLICK & CO. FROM DATA FURNISHED BY THE NATIONAL ASSOCIATION OF BUILDING OWNERS & MANAGERS




AVERAGE INTEREST RATE ON ALL MORTGAGE LOANS
MANHATTAN ISLAND
COMPARED WITH ST. LOUIS
AVERAGE INTEREST RATES
6.40
6.20
6.00
5.80
5.60
5.40
5.20
5.00
4.80
4.60
4.40
4.30
6.16
5.97
ST. LOUIS
MANHATTAN ISLAND
PANIC OF 1907
WORLD WAR I STARTS
ARMISTICE
STOCK MARKET COLLAPSE
BANK COLLAPSE
WORLD WAR II STARTS
V-E DAY
V-J DAY
4.95
4.93
4.92
4.64
1905
1910
1915
1920
1925
1930
1935
1940
1945
1950
PERCENTAGE
100
90
80
70
60
50
40
30
20
10
0
PERCENTAGE OF MORTGAGES MADE AT 5%
PERCENTAGE OF MORTGAGES MADE AT 6%
MADE AT 4½%
PERCENTAGE OF MORTGAGES
MADE AT VARYING INTEREST RATES
ON MANHATTAN ISLAND
1905
1910
1915
1920
1925
1930
1935
1940
1945
1950

OUTLOOK FOR OFFICE BUILDINGS GOOD

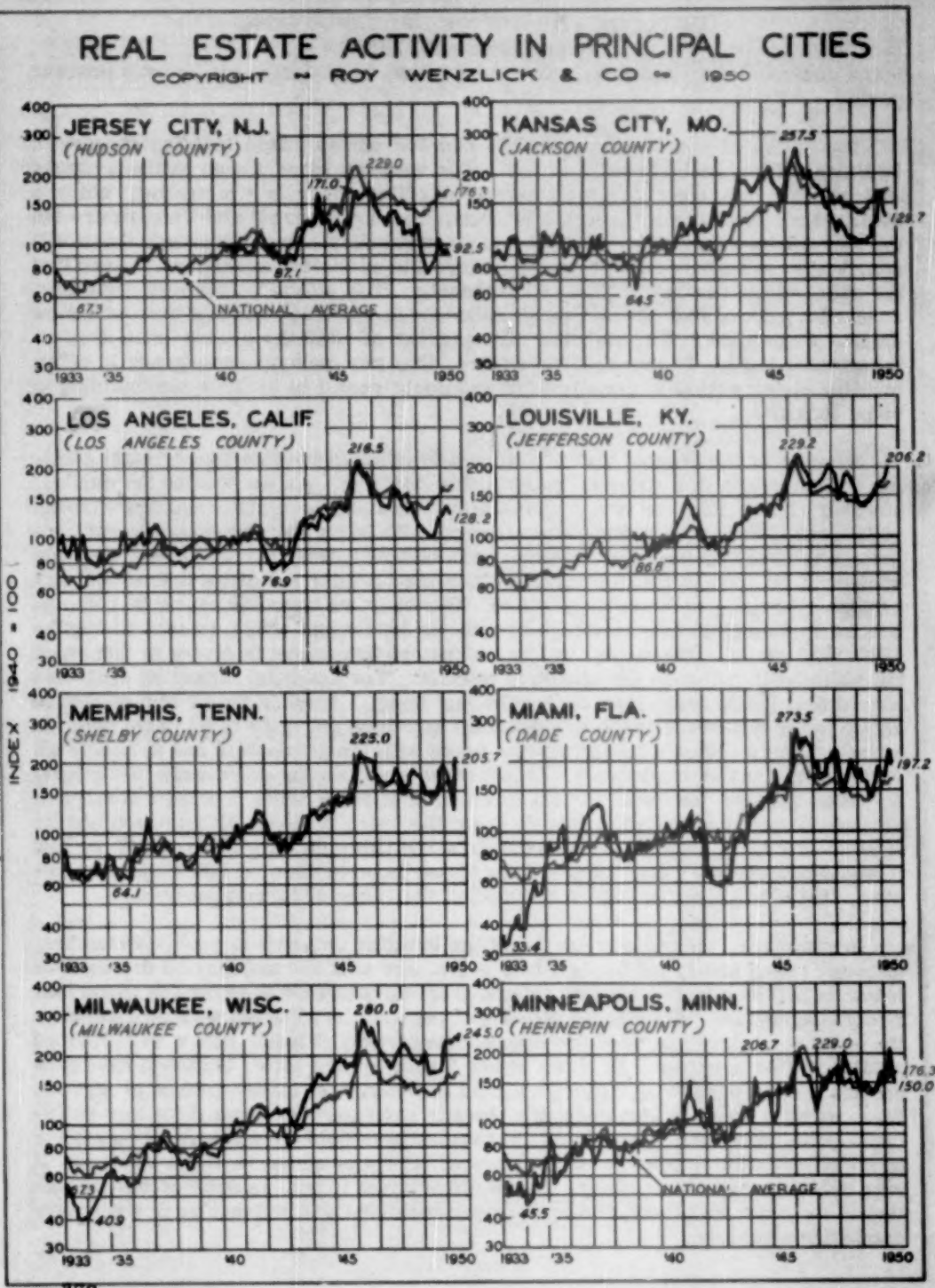
(cont. from page 365)

many offices, lofts, and warehouses as we have built during the present postwar period.

The group of charts on pages 366 and 367 shows office building vacancy in 56 United States and Canadian cities. The vacancy rates shown by these charts indicate that in some cities the scarcity of office space is diminishing, while in others the demand is still high. Boston, Denver, Detroit and Chicago are the top four cities among those with the highest vacancy rates. Although there will nearly always be some cities with demands for additional space, we believe that the nation-wide demand is finally slackening. The nation's business population reached a peak of four million establishments in mid-1948 and has been in a slow decline since then. Through the last quarter of 1949 the accumulated drop amounted to 1.3%. It appears, therefore, that any general resurgence in office building construction is uncalled for and could result in serious overbuilding in some localities.

Because of the present high cost of constructing new office space, most existing buildings are in a splendid competitive position. As we pointed out earlier, however, their position is not unassailable and can be maintained only through wide-awake, forward-looking management. We know that the management profession is probably weary of hearing about modernization, but we believe that this subject is so vital to the continued well-being of older buildings that almost any amount of harping on it seems justified. Our chart on page 365 shows that the incentive to construct new buildings is still far below that which existed during the 1925-1930 period. There are a number of factors that cannot be shown in this chart but which still influence the incentive to build. For example, financing costs are a good deal lower today than during the last boom. Another factor that cannot be shown is the difference in the new buildings and those put up 20 to 50 years ago. In some respects today's buildings are more efficiently planned and in nearly all respects are easier to maintain. On the other hand, zoning ordinances in virtually all cities require "setbacks" in the building as it rises above a certain number of stories, thereby frequently cutting down the ratio between office space and lot space. If it were possible to incorporate all of these factors in our incentive line it would undoubtedly cause the line to be higher than we show it. We believe, however, that it would not be higher than 65% of the 1925-1930 incentive level.

In summary, the outlook for the office building industry is good. Vacancies, although rising slowly for the last four years, are still low and may be driven even lower in certain cities as our new defense program brings about expansion of various Federal agencies. While some cities will possibly be afflicted with overbuilding, the older structures can meet this competition partway at least, with a well-planned modernization program. In cities where few or no new office buildings have gone up, the owners of existing buildings should also carry out modernization programs. When existing space is kept up to date there is naturally less demand for new buildings. It is, therefore, apparent that modernization should be of primary importance to all office building owners and managers. If the program is started in time, it may help forestall overbuilding. If new office space is built in spite of modernization of the older buildings, the modernized buildings will at least be in a stronger competitive position.

REAL ESTATE ACTIVITY IN PRINCIPAL CITIES

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